



Signed: February 14, 2009

Leslie Tchaikovsky

LESLIE TCHAIKOVSKY
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re

No. 08-40399 TG
Chapter 13

GANICE MORGAN-AUSTIN, DARREN
AUSTIN,

Debtors.

GANICE MORGAN-AUSTIN, DARREN
AUSTIN,

A.P. No. 09-4070 AT

Plaintiff,

vs.

PATELCO CREDIT UNION,

Defendant.

MEMORANDUM OF DECISION

The above-captioned chapter 13 debtors (the "Debtors") filed the above-captioned adversary proceeding, seeking to enjoin the foreclosure sale of their residence (the "Residence") by Patelco Credit Union ("Patelco"), the holder of a first deed of trust on the Residence. On February 9, 2009, the Court heard and granted a temporary restraining order, setting a hearing on the application for

1 a preliminary injunction for February 19, 2009 at 3:00 p.m. with
2 additional briefs to be filed by February 13, 2009. After reviewing
3 the evidence and argument submitted, including the reply briefs, the
4 Court concludes that a preliminary injunction should be issued
5 conditioned on satisfactory future payments being made. The reasons
6 for the Court's conclusion are set forth below. Given the nature of
7 the expedited relief sought, none of the findings of fact or
8 conclusions of law are final rulings and are controlling only for
9 purposes of this proceeding.

10 **SUMMARY OF FACTS AND PROCEDURAL HISTORY**

11 The Debtors filed a chapter 13 bankruptcy case on July 11, 2007,
12 Case No. 07-42148. Patelco obtained relief from the automatic stay
13 in this case on November 28, 2007. Patelco filed an objection to the
14 Debtors' plan. On December 15, 2007, an agreed order was filed
15 resolving the objection. On December 17, 2007, an order was entered
16 confirming the Debtors' plan. On December 17, 2007, a declaration
17 was filed by Patelco, stating that the Debtors were in breach of the
18 agreed order. On January 29, 2008, the Debtors filed a motion to
19 dismiss the bankruptcy case. The order was granted, and the case was
20 dismissed on January 11, 2008.

21 On January 29, 2008, the Debtors filed the above-captioned case.
22 On the same day, they filed a chapter 13 plan (the "Plan"). The Plan
23 proposed to pay the chapter 13 trustee \$1,000 per month for six
24 months and \$3,796 per month for fifty-four months. The Plan provided
25 that the Debtors would make the post-petition payments to Patelco
26 directly. The bankruptcy schedules, which were filed with the

1 petition, valued the Residence at \$990,000 with secured claims
2 equaling its value. The balance of Patelco's claim was scheduled as
3 \$733,000.

4 Because the Debtors had two cases pending within one year, the
5 automatic stay was due to expire 30 days from the petition date
6 unless extended by the Court. The Debtors filed a motion to extend
7 the automatic stay on February 8, 2008. Patelco filed an opposition
8 to the motion, and a hearing on the motion was scheduled for February
9 28, 2008. At the hearing, Patelco contended that the filing of the
10 current case violated 11 U.S.C. § 109(g) and had to be dismissed.
11 The Court agreed that the Debtors were required to establish changed
12 circumstances to maintain the case. The Debtors contended that Mrs.
13 Morgan-Austin, a real estate agent, had obtained additional
14 employment and that this constituted sufficient changed
15 circumstances.

16 At the conclusion of the hearing, as a condition of continuing
17 the automatic stay, the Court ordered the Debtors to provide evidence
18 to Patelco by March 7, 2008 of Mrs. Morgan-Austin's new employment.
19 If she failed to do so, the motion to extend the stay would be
20 denied. The Court further ordered that, if evidence were provided by
21 the specified date, the continuation of the automatic stay would be
22 further conditioned on the Debtors making the post-petition payments
23 when due or within the applicable grace period with a ten day notice
24 to cure in the event of a default. In addition, the Debtors were
25 required to pay \$10,000 to Patelco by April 28, 2008. There was no
26 grace period or ten day cure period with respect to this payment.

1 The Debtors were ordered to comply with all of the other terms of the
2 loan and security agreement.

3 Patelco asked the Court to allow this \$10,000 payment to be
4 applied to the pre-petition default in view of the prior case. The
5 Court refused to make this provision a condition of the order. There
6 was no discussion of conditioning the continuation of the automatic
7 stay on the Debtors remaining current to the chapter 13 trustee.
8 There was also no discussion of the amount of attorneys' fees to
9 which Patelco would be entitled in the event of a breach.

10 An adequate protection order was submitted to the Court on or
11 about April 16, 2008 (the "Adequate Protection Order"). The Debtors
12 did not object to the form of the Adequate Protection Order despite
13 the fact that it was inconsistent with the Court's oral order in at
14 least three respects: (1) the proposed Adequate Protection Order
15 provided that the \$10,000 payment would be applied to the pre-
16 petition default; (2) the Adequate Protection Order provided that
17 continuation of the stay would be conditioned on the Debtors
18 remaining current to the chapter 13 trustee;¹ and (3) the Adequate
19 Protection Order provided that, in the event of a breach of the
20 Order, the sum to cure the breach would include the sum of \$485 or,
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23 ¹Because this provision was improperly included in the
24 Adequate Protection Order, the Court will omit any discussion of
25 the Debtors' defaults based on their failure to keep their plan
26 payments current. However, the Court notes that hearings are
currently scheduled for March 20, 2009 on the chapter 13 trustee's
motion to dismiss the case on this ground and on the Debtors'
objection to the claim of Wells Fargo Bank, N.A., a junior secured
creditor on the Residence.

1 if Patelco obtained relief due to the breach, \$85 would be added to
2 the secured claim.

3 In the absence of an objection to the form of the Order, the
4 Court signed it without noting the discrepancies. An Amended
5 Adequate Protection Order was later submitted to the Court. It did
6 not correct the discrepancies nor did the Debtors object to its form
7 at this time either. The Amended Adequate Protection Order was
8 signed and entered on May 22, 2008 (hereinafter the "Adequate
9 Protection Order").

10 The Plan was confirmed on April 22, 2008. Patelco apparently
11 received adequate evidence of Mrs. Austin-Morgan's additional
12 employment and payment of \$10,000 by an acceptable date. However, on
13 May 23, 2008, Patelco filed a declaration re breach of the Adequate
14 Protection Order (the "May 23 Declaration Re Breach"). The May 23
15 Declaration Re Breach stated that the Debtors were in default of the
16 Adequate Protection Order: (1) by failing to make one of the bi-
17 monthly payments for March 2008 and all of the monthly payments for
18 April 2008 and May 2008, and (2) by failing to make the plan payments
19 to the chapter 13 trustee for April and May 2008. Including late
20 fees, the cure amount was stated to be \$9,468.50. The Debtors were
21 given ten days' notice to cure these defaults.

22 The Debtors filed an opposition to the May 23 Declaration Re
23 Breach. In the opposition, they asserted that they had mailed their
24 chapter 13 payments to Tennessee as instructed by the chapter 13
25 trustee. They noted that payments were withdrawn from their account
26 by Patelco on a bi-monthly basis in the amount of \$1,787. They

1 asserted that they could not determine the correct nature of the
2 default on the post-petition payments to Patelco as the amounts
3 stated by Patelco were not consistent with their records. They
4 surmised that Patelco might have increased the amount of their
5 monthly payments without giving them notice as required by the
6 promissory note (the "Note"). They asserted that they had sufficient
7 funds to cure any defaults once the correct amount had been
8 ascertained. No hearing was ever scheduled to resolve this dispute.
9 However, Patelco did not attempt to proceed with its foreclosure at
10 that time.

11 On November 19, 2008, Patelco filed a second declaration re
12 breach of the Adequate Protection Order ("November 19 Declaration Re
13 Breach"). The November 19 Declaration Re Breach stated that the
14 Debtors were in default for one of the bi-monthly payments for August
15 2008 payment and for all of the payments for September through
16 November 2008 for a total of \$12,508.30. Patelco also asserted that
17 the Debtors were in breach of the Adequate Protection Order as a
18 result of being delinquent on their plan payments due to the chapter
19 13 trustee for August through November 2008. Patelco issued a notice
20 of sale (the "Notice of Sale") on January 14, 2009, scheduling a
21 foreclosure sale of the Residence for February 11, 2009. The Debtors
22 filed this adversary proceeding against Patelco on February 3, 2009.

23 **DISCUSSION**

24 The complaint seeks damages, an accounting, an injunction, and
25 declaratory relief. The complaint and the application for a
26 temporary restraining order and preliminary injunction assert three

1 claims for relief. First, they contend that the Notice of Sale
2 violated Cal. Civ. Code Cal. Civ. Code § 2924.8. Second, they
3 contend that Patelco breached its contract with the Debtor by
4 increasing their monthly payment more frequently than permitted and
5 without giving them prior notice. Third, they contend that Patelco's
6 November 19 Declarations Re Breach overstated the cure amount, so
7 that the Debtors were not given an adequate opportunity to cure any
8 default. As a result, they contend Patelco is not entitled to relief
9 from the automatic stay. Instead, the Debtors should be given proper
10 notice of the cure amount and a reasonable opportunity to cure. The
11 Court will address each of these claims in turn.

12 **A. VALIDITY OF NOTICE OF SALE**

13 Because of the national epidemic of foreclosures on home
14 mortgages, in July 2008, the California legislature enacted emergency
15 legislation, requiring lenders to attempt to negotiate workout
16 agreements on loan defaults before commencing or continuing
17 foreclosure proceedings. See Cal. Civ. Code §§ 2923.5, 2923.6,
18 2924.8, and 2929.3. The legislation was effective immediately. The
19 legislation did not require lenders such as Patelco, who had already
20 recorded notices of default, to re-record those notices after
21 attempting to negotiate. However, it did require such lenders, who
22 had not yet recorded notices of sale, to attempt to negotiate before
23 recording a notice of sale. There is no dispute that Patelco made no
24 attempt to negotiate with the Debtors before recording Notice of Sale
25 on January 14, 2009.
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1 Patelco contends that the legislation exempted them from any
2 obligation to negotiate with the Debtors before recording a Notice of
3 Sale because the Debtors were at that time still debtors in a
4 bankruptcy case. The specific provision upon which they rely is Cal.
5 Civ. Code § 2923.5(h)(3) which states as follows:

6 (h) Subdivisions (a), (c), and (g) shall not
7 apply if any of the following occurs:

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 (3) The borrower has filed for bankruptcy, and
the proceedings have not been finalized.

10 It is undisputed that the Debtors' bankruptcy case was still pending
11 at the time Patelco recorded the Notice of Sale. The Debtors contend
12 that the exemption did not apply because the bankruptcy case had been
13 finalized as to Patelco. Patelco had obtained relief from the
14 automatic stay and had never filed a proof of claim in the case.
15 Patelco contends that the phrase is clear and exempts it from
16 compliance unless the bankruptcy case has been dismissed.

17 There is some appeal to the Debtors' argument. The exemption
18 may have been created in recognition of the difficulty created by the
19 automatic stay with respect communications between creditors and
20 debtors. Once the automatic stay has been vacated, the Debtors
21 contend, the exemption no longer serves any purpose. On the other
22 hand, Patelco argues instead that the exemption reflects the
23 legislature's recognition that the bankruptcy process provides an
24 adequate opportunity for negotiation.

25 The Court has no way to determine the legislature's intent in
26 this regard. It can only construe the statutory language as it would

1 be commonly understood. Doing so, the Court finds Patelco's
2 construction of the language more plausible. Therefore, the Court
3 concludes that Patelco did not violate Cal. Civ. Code § 2924.8 when
4 it recorded the Notice of Sale without first attempting to negotiate
5 with the Debtors.

6 **B. IMPROPER INCREASES OF INTEREST RATE**

7 The Debtors contend that Patelco breached their contract by
8 increasing the interest rate in a manner contrary to the terms of the
9 Note. The Note, which is dated January 16, 2004, calls for monthly
10 payments of \$3,573.80 beginning on March 1, 2004 with interest at the
11 yearly rate of 3.875%. Paragraph 4 of the Note provides that the
12 interest rate (and thus the monthly payments) will change on the
13 first day of February 2007 and every twelve months thereafter. It
14 provides further that the holder of the Note will deliver or mail to
15 the Debtors notice of any changes before the effective date of the
16 change, the notice to include the amount of the monthly payment.

17 The Debtors contend that no notice was given of a proposed
18 interest rate change on February 1, 2007. Instead, notice of a
19 change was provided on August 7, 2007, increasing their interest rate
20 to 5.8750% per year and their bi-monthly payment to \$2,211.56.
21 However, they contend that Patelco breached this provision of the
22 Note in February 2008, just after this bankruptcy case was filed, by
23 increasing the interest rate again, to 6.125% per year without any
24 prior notice. This caused the monthly payment to increase to
25 \$2,265.96. The bank statements for February 2008 through August 2008
26 reflect these increases.

1 Patelco has provided no evidence that prior notice was given of
2 this increase. Instead, Patelco has apparently agreed to back out
3 all interest rate increases including the increase of which it gave
4 notice on August 7, 2007.² Thus, this claim is apparently moot.

5 **C. INACCURACY OF DECLARATION RE BREACH**

6 The Debtors contend that the November 19 Declaration Re Breach
7 misstated the amount of the default and was thus invalid so that
8 Patelco does not have relief from the automatic stay. The Court
9 agrees. The problem appears to have been caused by Patelco's
10 improper inclusion in the Adequate Protection Order of a provision
11 the Court expressly disallowed at the February 28, 2008 hearing,
12 i.e., that the \$10,000 payment by the Debtors could be applied to the
13 pre-petition defaults.

14 The November 19 Declaration Re Breach stated that the Debtors
15 were three and one-half months delinquent on their post-petition
16 mortgage payments: i.e., a one-half payment for August 2008 and a
17 full payment for September through November 2008 for a total
18 delinquency of \$12,508.30. Attached to the declaration of Ester
19 Carino, Patelco's custodian of records, is an accounting of the
20 payments received from the Debtors from February 11 to November 19,
21 2008 ("Patelco's Accounting"). This period consists of ten months,
22 requiring twenty bi-monthly payments of \$1,786.90 each for a total of
23 \$35,738.00. Patelco's Accounting reflects the receipt during this
24 period of fourteen payments of \$1,786.90 each for a total of
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26 ²In January 2009, Patelco gave the Debtors notice that their
interest rate and thus their bi-monthly payment would decrease.

1 \$25,016.60.³ However, Patelco's Accounting does not reflect receipt
2 of the \$10,000 payment made by the Debtors on May 1, 2008, which was
3 presumably improperly applied to the pre-petition debt. If the
4 \$10,000 payment had been properly applied, the cure amount would have
5 been only \$721.40. Presumably, the Debtors could have made this
6 small cure payment in a timely fashion.

7 As it was, the Debtors attempted to cure this improper amount by
8 tendering a check for \$12,508.30. Unfortunately, due to a banking
9 error, the payment did not clear. Patelco refused to accept a later
10 tender of \$10,735. Either amount would have been significantly in
11 excess of the amount properly due, even when the first bi-monthly
12 payment for December 2008 is taken into account.

13 Thus, the Court concludes that the November 19 Declaration Re
14 Breach was invalid and that Patelco does not have relief from the
15 automatic stay. Moreover, the Court will direct Patelco to submit an
16 Second Amended Adequate Protection Order containing only those
17 provisions which the Court approved at the February 28, 2008 hearing.
18 A tape of the hearing may be obtained from the Court at a nominal
19 expense to ensure that the order submitted accurately reflects the
20 Court's ruling.⁴

22 ³In its calculations, the Court has relied on Patelco's
23 accounting of the payments made. In their reply brief, the Debtors
24 assert that this accounting does not given them credit for various
25 payments and overpayments made from May to August 2008. The bank
statements support this assertion. Patelco should clarify this
apparent discrepancy.

26 ⁴In its reply brief, Patelco again relies in part on the
Debtors' default with respect to the case in general. Since there
should not have been a provision in the Adequate Protection Order

1 Since Patelco has refused the Debtors' recent tenders of cure
2 payments, the Debtors are now in default of additional post-petition
3 payments. The Court directs the Debtors to be prepared to make a
4 reasonable proposal for cure of these payments at the hearing on
5 February 19, 2009.

6
7 **CONCLUSION**

8 For purposes of this application, the Court concludes that the
9 Notice of Sale was not invalid based Patelco's failure to comply with
10 the provisions of Cal. Civ. Code § 2924.8. The Court concludes that
11 Patelco's breach of contract claim based on improper rate increases
12 is moot. Finally, the Court concludes that the November 19
13 Declaration Re Breach grossly overstated the cure amount so that
14 Patelco is not entitled to relief from the automatic stay and that
15 the Adequate Protection Order significantly misstated the Court's
16 oral order and should be amended. The application will be granted on
17 conditions to be set at the February 19, 2009 hearing.

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requiring the Debtors to maintain payments to the chapter 13
trustee, these defaults will be addressed at the hearing on the
trustee's motion to dismiss the case rather than as part of this
adversary proceeding. Moreover, it is not clear to the Court to
what extent Patelco's improper application of the \$10,000 may have
contributed to the Debtors' defaults to the trustee.

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